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Major Industrial Countries Agree Dollar Has Fallen Enough

Finance ministers and central bankers from six major industrial countries agreed February 22 that currency values are now "broadly consistent with underlying economic fundamentals" and that a further decline in the dollar would hurt the world economy. The accord, in effect, is the reverse of the September 22, 1985 agreement by the Group of Five (United States, Japan, West Germany, France and Britain) that the dollar was overvalued. Last weekend's discussions in Paris added Canada to the original group. (Italy, which had been expected to participate as a member of the Group of Seven, boycotted the final meeting to protest its exclusion from the preliminary Group of Five meeting on February 21.)

The agreement, which followed weeks of private negotiations, resembled the October 31, 1986 accord negotiated by Treasury Secretary James Baker and Japan's Finance Minister Kiichi Miyazawa (see JEI Report No. 41B, November 7,

Such statements underscore the rift between the congressional and executive approaches to sectoral trade issues. White House officials have said that the president will oppose attempts to protect specific sectors -- a warning that Congress may have to try to override another veto. Last year the House fell eight votes short (see JEI Report No. 30B, August 15, 1986). Given the milder provisions of S 549/HR 1154, Congress may have better luck this year.

Eileen Marie Doherty

The 1986 U.S. Trade Account: Looking For The Silver Lining

Is the worst of the U.S. trade problem over? Reagan administration trade policymakers and business economists alike are convinced that the gap between imports and exports this year will be narrower than 1986's red-ink entry of $169.8 billion (imports valued c.i.f.). But undoing four years of runaway growth in this country's trade deficit will be slow work, they caution. Even with the big drop in the dollar's value since February 1985, it will be difficult to trim the 1987 number to 1985's $148.5 billion shortfall.

A glance at the 1986 export and import figures indicates why otherwise optimistic White House economists are reluctant to predict a major turnaround in the U.S. trade account. Exports increased by a scant 2 percent last year to $217.3 billion -- or roughly 1984's level, itself $15.9 billion shy of the record set in 1981. Moreover, shipments were barely higher in the second half of 1986 than in the first six months for reasons that have a familiar ring -- the weak economic performance turned in by other industrialized nations, the debt problems of many developing countries, and the reduced revenues of oil exporters. These factors will continue to offset some of the benefits of the lower dollar in 1987. Still, the prospects for exports look better than at any time in the past five years.

The other side of the equation is a bigger question mark. At $387.1 billion in 1986, U.S. imports were up by just 7 percent -- the second year of single-digit growth. Duplicating this record in 1987 will be much harder. For one thing, the huge drop in world oil prices that helped to contain the expansion of 1986 imports was a one-time break; prices this year are expected to average a dollar or two higher. What's more, Japanese and European manufacturers will be under more pressure in 1987 to hike prices on U.S.-bound exports to reflect the steep appreciation of their currencies. Last year most foreign suppliers opted to sacrifice short-term profits for market share, but this sales strategy has obvious limits. These two factors alone guarantee a bigger gain in imports than in 1985 and 1986. How much more depends on whether the U.S. economy continues to muddle along for the whole year or, as most economists project, picks up some steam in 1987's second half.

Analysts searching for hard evidence that the U.S. trade deficit has finally bottomed out can find several pieces in an unexpected place -- the 1986 data on trade with Japan. The already yawning gap between imports and exports admittedly widened from $49.8 billion in 1985 to $58.6 billion last year (imports again valued c.i.f.), but this number masked some encouraging trends, particularly in exports.

U.S. Exports to Japan

(in millions of dollars, f.a.s. value basis)

	January-December 1985	January-December 1986	Percent Change
Total Exports	$22,630.8	$26,881.6	18.8%
Industrial Supplies	8,679.9	8,751.5	0.8
Bituminous Coal	769.1	554.7	-27.9
Petroleum Products	762.0	567.7	-25.5
Natural Gas	249.1	187.0	-24.9
Nuclear Fuels	121.5	28.7	-76.4
Logs and Lumber	884.9	1,097.4	24.0
Paper Base Stocks	470.2	563.8	19.9
Paper and Paper Products	288.9	354.0	22.5
Organic Chemicals	704.0	731.8	3.9
Inorganic Chemicals	801.9	883.9	10.2
Plastics and Synthetic Resin Compounds	305.6	322.0	5.4
Manufactured Fertilizers and Insecticides	243.1	246.1	1.2
Steel Scrap	199.1	170.0	-14.6
Nonferrous Ores and Scrap	459.6	491.8	7.0
Nonferrous Metals	289.4	205.8	-28.9
Textiles	107.5	121.7	13.2
Raw Cotton	368.0	238.6	-35.2
Hides and Skins	298.2	331.4	11.1
Leaf Tobacco	302.4	227.1	-24.9
Capital Goods	5,938.6	6,727.5	13.3
Nonelectric Machinery	3,384.7	3,561.7	5.2
Data Processing Equipment	1,331.1	1,400.6	5.2
Measuring, Testing and Control Instruments	448.7	477.2	6.4
Laboratory Testing and Control Instruments	104.5	103.9	-0.6
Scientific, Professional and Medical Equipment	265.5	337.0	26.9
Metalworking Equipment	113.9	143.0	25.5
Service Industry Equipment	120.1	143.7	19.7
Electric Machinery	804.3	977.5	21.5
Generators and Transformers	75.9	73.7	-2.9
Broadcast and Communications Equipment	327.1	402.8	23.1
Telephonic and Other Electric Equipment	401.3	500.9	24.8
Transportation Equipment	1,749.6	2,188.3	25.1
Civilian Aircraft	905.9	1,161.3	28.2
Civilian Aircraft Engines and Parts	552.1	659.6	19.5
Automotive Parts	214.8	235.0	9.4
Food and Feed	5,000.7	5,042.8	0.8
Corn	1,305.3	878.0	-32.7
Sorghum	242.9	178.0	-26.7
Soybeans	937.7	838.8	-10.5
Wheat	469.0	424.3	-9.5

Fruits and Vegetables	452.1	584.0	29.2
Meat and Meat Products	540.8	760.9	40.7
Fish and Fish Products	685.4	864.2	26.1
Consumer Goods	1,415.5	1,689.9	19.4
Pharmaceuticals	590.5	647.4	9.6
Toys and Sporting Goods	79.7	98.0	23.0
Cigarettes	94.9	128.0	34.9

U.S. Imports from Japan

(in millions of dollars, Customs value basis)

	January-December 1985	January-December 1986	Percent Change
Total Imports	$68,782.9	$81,911.1	19.1%
Automotive Products	24,980.0	32,849.1	31.5
Cars	16,231.3	21,060.7	29.8
Assembled Trucks	4,311.6	5,713.4	32.5
Automotive Parts	4,429.5	6,065.6	36.9
Capital Goods	21,515.7	25,333.9	17.7
Nonelectric Machinery	14,448.9	17,230.9	19.3
Business Machines	6,274.1	7,901.9	25.9
Metalworking Machinery	1,238.7	1,475.3	19.1
Specialized Industrial Machinery	1,323.1	1,598.0	20.8
Scientific, Professional and Medical Equipment	670.0	835.2	24.7
Electric Machinery	6,542.6	7,532.5	15.1
Transportation Equipment	524.2	570.5	8.8
Consumer Goods	14,017.2	15,451.1	10.2
Video and Audio Recorders and Players and Stereo Equipment	5,280.1	5,881.1	11.4
Television Sets	827.7	869.0	5.0
Radio Receivers	306.9	272.9	-11.1
Tableware and Glassware	442.8	453.8	2.5
Metal Cookware and Cutlery	438.3	473.0	7.9
Photographic and Optical Goods	918.5	1,164.8	26.8
Clocks and Watches	479.9	477.2	-0.6
Toys and Sporting Goods	563.8	523.1	-7.2
Motorcycles and Parts	883.8	853.3	3.5
Clothing	487.3	464.0	-4.8
Intermediate Goods	7,035.3	6,948.7	-1.2
Steel Mill Products	3,048.3	2,231.5	-26.8
Nonferrous Metals	535.0	504.6	-5.7
Organic Chemicals	564.1	732.2	29.8
Textiles	715.2	855.4	19.6

On paper, U.S. shipments to Japan increased by a whopping 18.8 percent in 1986 to $26.9 billion despite generally lower prices for the agricultural and industrial inputs that make up just under half of total exports. As has been well publicized, most of this gain was illusary, reflecting transshipments of foreign gold through the United States to Japan. Still, sales of industrial supplies, food and feed, capital goods and consumer goods did expand by a solid 5.6 percent to a new record level. More importantly, all of this gain occurred in 1986's second half; at mid-year exports were actually running 4.1 percent behind their year-earlier tally. With the Japanese economy continuing to struggle during the July-December period, this turnaround is strong proof that the weaker dollar has at last begun to boost U.S. exports.

It is more difficult to build a case that the expansion of imports from Japan has peaked. The rollback in the growth rate from 19.9 percent in 1985 to 18.1 percent last year, when purchases hit $85.5 billion, is certainly too slight to draw any conclusions, particularly given the fact that so much of the trade is distorted by restraint arrangements. There were some scattered signs that the volume gains that had propelled imports up in the first half of 1986 were less of a driving force in the second half. But whether this change reflected the sluggish pace of U.S. growth or the J-curve effect will only become clear this year.

Susan MacKnight

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The views expressed in this report are those of the authors and do not necessarily represent those of the Japan Economic Institute.